PROCEDURE NO.

803 Making an Initial Valuation of Property and Equipment

The following guidance is included for the benefit of those LEAs that have not previously maintained a General Fixed Asset Account Group and those that have not yet implemented the new governmental reporting model established by GASB 34. In the new reporting model, the General Fixed Asset Account Group is eliminated. Instead, capital assets are reported in the government-wide statement of net assets, and a schedule of capital assets is included in the notes to the financial statements. The following methods for initial valuation of property and equipment apply to either model.

Most of the information needed to prepare an inventory listing (description, name, identification number, and so forth) of the fixed assets of the LEA is available by locating the asset. However, if the asset was not purchased recently, information on the cost may not be available.

Generally accepted accounting principles for all business enterprises, including LEAs and other public agencies, have always required the use of "historical cost" to measure an entity's investment in property and equipment.

Historical cost simply means actual cost at the time of acquisition. Actual cost includes the invoice cost of the item, plus any applicable sales tax, freight, or installation charges. Such actual cost represents the value to be recovered over the useful life of the asset through depreciation. When items are disposed of in any manner, they are removed at actual cost. Any accumulated depreciation is also removed from the depreciation allowance account.

In the past, LEAs and other public agencies, since they typically did not need to compute depreciation, had not been concerned with historical costs of property and equipment and have charged these costs to the expenditure budget in the year of acquisition. (Note that depreciation was recorded in proprietary funds.) The LEA's primary concern has been that of accountability for the item and valuation for insurance purposes. As a general rule, therefore, LEAs have not maintained fixed assets ledgers for the purpose of recording the actual historical cost of property and equipment. This changes with the advent of the Governmental Accounting Standards Board (GASB) Statement 34, *Basic Financial Statements—and Management's Discussion and Analysis—For State and Local Governments.* LEAs will be required to report their capital assets in their government-wide financial statements. GASB Statement 34 becomes effective in three phases based on LEAs' total annual revenues. The largest LEAs must implement first for the 2001-02 fiscal year. For more information, please see CDE's Web site at http://www.cde.ca.gov/fiscal/financial/financial.htm.

State legislation requiring inventories of property and equipment and the exceptions taken by independent auditors have focused attention on this omission of fixed assets information in the LEA's books and financial statements. LEAs have found that establishing valuation for inventory purposes has been difficult because of the lack of historical records. Legislation now calls for a "reasonable estimate" if cost is not available, and LEAs and their auditors are afforded a starting point that should be acceptable. It should be noted that under GASB Statement 34, if assets and depreciation are omitted from the financial statements, the LEA might receive an adverse opinion on the financial statements from its auditor. An adverse opinion means that the financial statements are not presented fairly in conformity with generally accepted accounting principles.

Valuation of existing inventory of property and equipment can be made on the basis of (1) actual cost of each item, if records are available to support such costs; or (2) appraised/estimated cost based on the time of acquisition.

The following guidelines are to be used in determining the method of valuation for inventory purposes:

1. Actual cost

   The actual cost should include the invoice cost paid by the LEA, plus tax, freight, or other form of transportation for delivery to the LEA, whether added to the invoice or paid separately to a carrier. To this cost the LEA should add any labor and other costs of installation. Labor and other costs of installation by the vendor will usually be included in the original invoice price or billed separately by the vendor.

2. Appraised/estimated cost

   a. Appraised acquisition cost—LEAs may find it desirable to employ an outside agency to set up an inventory and/or update it. Some appraisal companies have the ability to compute the estimated cost based on the estimated date of acquisition of the particular items. Costs developed in this manner would be acceptable in either establishing a new inventory or adding to the inventory items which may have been missed in the establishment of the initial inventory. Use of an appraisal service also has the additional advantage of developing current market values for insurance purposes, either on a replacement-cost basis or a depreciated-replacement-cost basis. Once the inventory listing is established, it is necessary to update it for current-year purchases and disposals of fixed assets. For insurance purposes it is advisable to maintain current market values.

b. Reasonable estimate of cost—If the original acquisition cost cannot be traced through the LEA's records, a reasonable estimate of original acquisition cost may be used. Methods of determining such reasonable estimates of cost are many and varied. It is important for auditing purposes that the methods employed be carefully documented. While it is not necessary to use the same method for each item, the methods should be designed to produce a consistent result. Care should be exercised in the establishment of each item's cost. Among the methods that may be employed are the following:

   (1) Compare the item to a similar one of more recent acquisition for which you have a price. Adjust that price through a formula that would eliminate the effect of inflation/deflation for the number of years the older item has been in your possession.
   (2) Research bid files for bids on similar items and apply any necessary inflation adjustments.
   (3) Seek assistance from vendors who manufacture or sell items similar to the items you are attempting to price.
   (4) Check with other LEAs that may have purchased similar items.

Any other method which can be shown to reflect a reasonable estimate of the original acquisition cost of the item may also be used.

In accepting donated items, the LEA's governing board should approve the valuations based on their fair market values as of the dates of acceptance.